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SUBJECT: ESTONIA ON ECON CRISIS: TRUST THE FREE MARKET

Classified By: Charge Karen Decker for reasons 1.4 (b) and (d)

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¶1. (C) SUMMARY: In a March 24 meeting with Econoff, Ministry of Finance (MOF), Central Bank and MFA officials concurred with most reftel points on the financial crisis, but noted that they do not feel the EU needs to increase the size of its stimulus package. GOE officials question whether the IMF fundamentally understands the dynamics of this crisis, or if the Fund is inconsistently and incorrectly applying the lessons of the Asian financial crisis. Estonia remains committed to market solutions, and notes excellent support from, and cooperation with, Swedish banks. The GOE's timeline for Euro accession is January 1, 2011, and it is looking for a clear signal from the EU that it believes Estonia can meet this target. END SUMMARY

¶2. (C) On March 18, the Charge communicated reftel points to Estonia's Minister of Finance Ivari Padar. Then on March 24, Econoff had a follow-up meeting with Andres Sutt, Deputy Governor of the Bank of Estonia (BOE), Tanel Ross, Head of International Relations for BOE, Martin Poder, MOF's Head of EU and International Affairs, Mart Kivine, Advisor to the Minister of Finance, and the MFA's U.S. Desk Officer. GOE officials expressed clear support for the broad themes (contained in Ref A) of U.S.-EU cooperation, anti-protectionism, and the need to support both home bank headquarters as well as regional subsidiaries (a major point of interest in Estonia where all major banks are subsidiaries of Swedish or Danish banks). They received our points as a welcome sign of the Administration's commitment to working with Europe to get out of the present crisis. With respect to these themes, GOE officials made the following points:

-- It is important that bank balance sheets be cleaned up as quickly as possible, but also that the financial system not end up publicly owned, especially as more countries are lining up for aid;

-- Estonia is not in a position to contribute to the expansion of the new arrangements to borrow (NAB), as the GOE has already committed resources to the IMF support package for Latvia. Noting that the "greater Nordic economy" was the only major economic region of the world left out of the G-20, Deputy BOE Governor Sutt and wondered if repeated meetings to manage the financial crisis might in fact bring on more instability than they solve.

-- The MOF and BOE are concerned about abrupt exchange rate swings among EU member currencies outside the Euro zone, as this puts additional pressure even on countries inside the Euro zone who are less competitive.

¶3. (C) On regional and/or EU cooperation, and IMF involvement:

-- The group noted Estonia's excellent communication with Sweden's Riksbank and Swedbank to give support to the Baltics. These banks, in particular, recognize the nuances that exist among the Baltic

countries' economies (Ref C).

-- There are signs that the market is differentiating Estonia from its neighbors, but some EU discussions of the crisis still tend to blur the whole region together, based on the lowest common denominator economy. More needs to be done to seek a regional approach to the crisis.

-- Sutt remarked on the Fund's lack of consistency, noting the markedly different conditions applied to Latvia compared with Belarus. He also noted Lithuania's concern that seeking an IMF package could signal insolvency, when its real problem is liquidity.

¶4. (C) On fiscal stimulus:

-- All agreed that the current EU approach contains sufficient nuance. The GOE does not believe a traditional Keynesian approach of countries spending their way out of the crisis will work for the small, open, newer EU economies.

-- Overall, they feel the EU has allocated the right amount of stimulus. Kivine of MOF commented that Estonia, for example, cannot afford to spend its way into an 11 percent of GDP budget deficit the way Euro zone member Ireland has.

¶5. (C) On Estonia's path to Euro accession:

-- Kivine and Sutt both downplayed PM Ansip's recent statements in Brussels that Estonia could be ready to adopt the Euro as early as ¶2010. Kivine said this idea was "just being played with" and that recent press reports of the European Central Bank's displeasure with the GOE were "blown out of proportion." The GOE does not expect Euro

accession before January 1, 2011 and "there is no discord on this," Kivine said. Sutt added that accession 4-6 months earlier would not make a difference. More important, he said, is that Estonia get a clear signal soon from the European Central Bank (ECB) and the European Commission that they believe Estonia can meet the Maastricht criteria for accession by 2011.

¶6. (C) COMMENT: Throughout the meeting, there were signs of some fatigue with the ongoing focus on Central and Eastern Europe. Sutt and Kivine touched on previous critiques (Ref D) that the IMF seems stuck with an "Asian model" focused on exports, savings and current account surpluses. He also wondered whether IMF staff grasp the fundamental differences between the Asian crisis and the current one. The group noted they see this crisis as one that began in mature economies, driven by huge imbalances, which must be corrected. They acknowledged that in this climate, states with weaker fundamentals are at risk. Within the EU, the GOE will continue to stress faith in the free market - as much as possible - to resolve the current crisis.

DECKER